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GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF LICENSING AND REGULATORY AFFAIRS
FINANCE AND ADMINISTRATIVE SERVICES
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emailed 6/1/12 (ael)

June 1, 2012

Mr. Doug Ringler, Director
Office of Internal Audit Services
State Budget Office
Romney Building – Seventh Floor
111 S. Capitol, P.O. Box 30026
Lansing, Michigan 48909

Dear Mr. Ringler:

We are enclosing our response to comments made in the Office of the Auditor General's Performance Audit of the Collection of Delinquent Unemployment Taxes and Reimbursements, Unemployment Insurance Agency, Department of Licensing and Regulatory Affairs for the period October 1, 2008 through June 30, 2011.

If you have any questions regarding this report, please feel free to call me at (517) 335-9247.

Sincerely,

(SIGNED)

Allen Williams, Director
Office of Audit & Financial Compliance

Enclosure

cc: Distribution List
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AUDIT RESPONSE SUMMARY

Performance Audit of the Collection of Delinquent Unemployment Taxes and Reimbursements

Unemployment Insurance Agency Department of Licensing and Regulatory Affairs (October 1, 2008 through June 30, 2011)

I. Citations complied with:

None

II. Citations to be complied with:

- # 1. Corrective action is underway – we expect full compliance by August 13, 2012
- # 2. Corrective action is underway – we expect full compliance by August 31, 2012
- # 3. Corrective action is underway – we expect full compliance by August 13, 2012
- # 4. Corrective action is underway – we expect full compliance by January 1, 2013
- # 5. Corrective action is underway – we expect full compliance by January 1, 2013
- # 6. Corrective action is underway – we expect full compliance by January 1, 2013

III. Citations agency disagrees with:

None

Audit Response
Unemployment Insurance Agency
Department of Licensing and Regulatory Affairs

A. Completed Improvements

1. **New Estimation Process for Unpaid SUTA Taxes:** The Agency has developed and implemented a new estimation process for unpaid SUTA taxes effective November 1, 2011. This new process uses the actual gross and taxable wages from the same quarter of prior year's tax report filed by the employer as wages for the estimated report. This change provides a reasonable and substantiated basis for estimating tax liabilities without overstating the receivables while also preserving the integrity of the tax rate calculation.

B. Improvements Under Development

1. **Collection Procedures:** Post audit, all collection procedures were reviewed, updated and submitted to the Agency Director on March 16, 2012. These collection procedures will go through a clearance process with the Agency's Attorney General and are planned to be effective immediately after that review. A copy of final procedures will be transmitted to the OAG when completed.
2. **Best Practices Review and Plan:** A Project Control Office (PCO) has been created as an adjunct to the UIA-IS Project Management Office. The PCO has procured a personnel expert in UI practices and tasked them to a) review UIA's current business processes, b) identify and document nationally recognized best practices, and c) create a change plan for UIA business process to incorporate best practices. This effort began April 4, 2011.
3. **Computer System:** The back-bone of the UIA's computer system is a 25 year old, Cobol programmed, mainframe system which results in a loss of productivity, efficiency, and agility. The functional requirements of the new system will address many of the conditions cited in the Audit and improve collections and quality control. The DTMB-selected vendor has committed to complete the tax portion by August 13, 2012 and the benefit portion by December 31, 2013.

FINDING #1 – Collection Efforts for Delinquent SUTA Taxes

Auditor General Recommendation:

We recommend that UIA's CU and TEU initiate sufficient and timely efforts to collect delinquent SUTA taxes from contributing employers.

Process/Procedures/Training:

Strategy	Completion Date
Conduct a review of the collections process and procedures for both Collections and TEU. Included in this review will be a Collections workload study.	Completed
Provide refresher training to all Collections staff that all collection activities, including phone contacts, must be recorded in the employer's Account History.	Completed
Develop guidelines, including timelines, detailing when delinquent accounts will be forwarded from Collections to TEU.	Completed
Add 10 collections staff to detect delinquencies earlier.	Completed

Performance Metrics:

- A new collection customer service unit was started on March 5, 2012 that will make the initial call to delinquent employers within one month of being delinquent. All delinquent employers will be referred to the Collections Unit if payment is not received in full at the time of the phone call.
- The updated collection procedures were finalized on March 20, 2012. A collections workload study was also conducted for calendar year 2011. As of December 31, 2011, there were 105,586 delinquent accounts; 49,590 employers were active and 55,996 were inactive. In addition, 14,280 employers out of the 105,586 properly reported but did not pay their entire balance in full; the remaining 91,306 did not file a quarterly or pay any amount.
- The current ratio of delinquent accounts to collector is 20,568:1. As a result of the above workload study, the Collections Unit is under review for staff additions and/reorganization to be completed concurrently with the change-over to the new computer system in August, 2012.
- In December, 2011, all collectors were given procedures on annotating the employer account history. Supervision has noted a 75% improvement in account history annotations since distribution.
- In January, 2012, a new procedure was added to the CU Work Flow Chart specifying when CU would transfer accounts to TEU for collection. An additional procedure was developed stating when CU will refer accounts to TEU for investigation, but not collection. CU would continue collections efforts after the investigation is completed. Trust Fund Management will provide oversight to ensure that procedures are being followed and working as intended.

FINDING #2 – Real Property Liens

Auditor General Recommendation:

We recommend that CU determine if delinquent contributing employers own real property before CU files real property liens against the employers.

We also recommend that CU establish controls to verify that county register of deeds offices promptly record UIA's liens and lien discharges and that CU documents the lien recording and discharge information in UIA's records.

IT:

Strategy	Completion Date
Pursue a computerized solution to determine if employer's real property exists in a county before creating a lien. This is part of the system rewrite project.	August 13, 2012

Process/Procedures/Training:

Strategy	Completion Date
Implement a new process to check the Consolidated Lead Evaluation and Reporting (CLEAR) public records for real property before the issuance of all manual liens.	Completed
Discontinue filing liens in Wayne County for employers whose business address on file with the UIA is outside the State of Michigan.	Completed
Pursue the electronic exchange of liens and recording information with Michigan counties.	August 31, 2012

Performance Metrics:

- The CLEAR System database was installed on five computers in the CU. Five account examiners were trained on the CLEAR System on December 8, 2011, and delinquent employers have been tracked since.
- Since requiring all collectors to access the CLEAR System to verify that real property exists, 100% of all manual liens have been processed correctly based on the real property results.
- By discontinuing filing liens in Wayne County for employers whose business is outside the State of Michigan, the number of liens processed has decreased by 10.8%. There were 2,130 December, 2011 liens filed but only 1,900 February, 2012 liens filed after removing the out of state employers.
- All 83 counties have been contacted to improve lien recording methods and lien payment methods. As of February 25, 2012, CU has secured a commitment from the five largest Michigan counties to accept electronically recorded liens and payment by credit card. This process will be fully implemented by August 31, 2012.
- Performance metrics will be developed after the electronic exchange of information is finalized with all Michigan counties.

FINDING #3 – Use of Information

Auditor General Recommendation:

We recommend that UIA use available data and data analysis resources to proactively identify and investigate employers potentially involved in SUTA dumping, potentially misclassifying some or all of their employees as independent contractors, in bankruptcy, or not registering with UIA.

IT:

Strategy	Completion Date
Develop a data sharing agreement with the Michigan Department of Treasury to access their registration data for cross-match verification purposes. Methodology to perform this cross-match is being developed in the system rewrite project.	August 13, 2012

Process/Procedures/Training:

Strategy	Completion Date
Develop a listing of industries to audit based on prior year's audit adjustments related to employee misclassification. Use this data along with SDDS software and IRS data to identify those industries/employers to target.	Complete
Conduct a study on how to best use the federal Judiciary's PACER database to timely identify the Michigan employers that filed for bankruptcy protection.	Complete

Performance Metrics:

- Targeted and IRS identified employers began being audited on January 1, 2012 by the Field Audit Unit. Field Audit Management will compare 2011 and 2012 data after six and twelve months and adjust as needed.
- Weekly monitoring of the PACER database has effectively identified new employers filing bankruptcy. A new guideline was implemented requiring each Bankruptcy collector to file a claim on a new case within one week of the employer appearing on PACER.

FINDING #4 – SUTA Tax Account Actions

Auditor General Recommendation:

We recommend that UIA's Tax Office timely initiate actions affecting contributing employers' SUTA tax accounts.

We also recommend that UIA's Tax Office ensure that UIA's master files contain up-to-date information.

IT:

Strategy	Completion Date
Develop an automated random selection process of determinations issued to verify accuracy and completeness. This is part of the system rewrite project.	August 13, 2012

Process/Procedures/Training:

Strategy	Completion Date
Begin processing SUTA dumping cases on a first in, first out basis.	Complete
Develop timeliness standards regarding the issuance of SUTA related liability determinations and assessments.	Complete
Develop and implement new controls to ensure all employers liable for delinquent SUTA taxes are referred to the Collection Unit. Liability examiners have been provided with instructions on following existing referral procedures. Additionally, as part of the system rewrite, predecessor debts will automatically be transferred to the successor to ensure accurate posting of the receivables.	Complete
Develop and implement new controls to ensure that the employer's master files contain up-to-date information. As part of the system rewrite, a new automated audit trail will track the entry of all updated employer information in the master files.	In-place & Ongoing
Develop a program to encourage all employers to expand their use of the UIA's on-line services.	January 1, 2013

Performance Metrics:

- SUTA determinations will be issued within 30 – 45 calendar days from the date the final recommendation is launched in the workflow system.
- A new collection customer service unit was started on March 5, 2012 that will make the initial call to delinquent employers within one month of being delinquent. All delinquent employers will be referred to the Collections Unit if payment is not received in full at the time of the phone call. (Also mentioned in Finding #1 Performance Metric.)
- The UIA will conduct more than 40 employer seminars statewide in 2012 and will educate and encourage employers to use the Agency's on-line services.

- Performance metrics to verify the accuracy and completeness of determinations will be developed once the tax system rewrite is implemented.
- PA 269 of 2011 requires employers to have on-line accounts with the Agency beginning January, 2013.

FINDING #5 – Estimation of Unpaid SUTA Taxes

Auditor General Recommendation:

We recommend that CU effectively determine if employers remain in business before estimating and attempting to collect employers' unpaid SUTA taxes.

We also recommend that CU accurately estimate employers' unpaid SUTA taxes using the employers' taxable wages.

Process/Procedures/Training:

Strategy	Completion Date
Research potential sources of information which would help automate the determination if employers are currently in business.	In Place & Ongoing
Develop a new estimation process using the employer's taxable wages to more accurately estimate employer's unpaid SUTA taxes.	Complete

Performance Metrics:

- Currently, for all delinquent employers, the Treasury Data Base and the LARA Entity Search is reviewed to determine if the current business status is active or inactive.
- A new estimation process was developed in which the UIA uses the employer's last year's taxable wages as the base for this year's estimated taxable wages. Due to the new estimation process, estimates for accounts receivable will decrease, but be more accurate. CU will compare last year's total receivables to this year's after first quarter 2012 reports are processed.

FINDING #6 – Security Collateral

Auditor General Recommendation:

We recommend that UIA ensure that applicable reimbursing employers provide UIA with security collateral.

Process/Procedures/Training:

Strategy	Completion Date
Convert all active reimbursing employers who are delinquent for two consecutive calendar quarters and failed to provide the security requirement, to “contributing” status.	Internal Policy - Ongoing
Cash in collaterals when a reimbursing employer is delinquent for two consecutive quarters, in addition to converting to contributing status.	Internal Policy - Ongoing

Performance Metrics:

- Conversions will continue as delinquencies develop. Any employer that does not pay for two consecutive quarters is converted to contributing status and also referred to the collections unit.
- Once the delinquency reaches \$10,000.00, the surety bond will be cashed in.